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SUBJECT: Mexico Economic Weekly - October 23

[1](#)1. (U) The Mexico Economic Weekly supplements reporting from Mission Mexico Consulates and the Embassy Mexico Economic Section to provide a sense of ongoing trends. Please contact Adam Shub (shubam@state.gov) or Sigrid Emrich (emrichs@state.gov) for questions or comments about this report.

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ECONOMY AND FINANCE

13. (SBU) As rating companies consider downgrading Mexican debt, the Senate now takes up the 2010 Revenue Bill that the Mexican Chamber of Deputies amended and approved October 20. While the Senate usually acts in a more conservative manner, Senators are divided over whether to accept the Chamber's increase in VAT taxes. The Chamber made considerable changes to the Calderon Administration's original proposal, modifying tax rates and tax laws designed to strengthen public finances and avert a credit rating downgrade. The Chamber scrapped the GOM's proposed 2% anti-poverty sales tax, but increased the VAT by 1% (to 16% and 11% at the border), keeping a zero rate for food and medicine. The Chamber also approved raising income taxes to 30%, up from 28%. The forecast for the average export price of Mexican oil was also increased to US\$59/barrel (from US\$53.9) and the

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on-balance sheet fiscal deficit was raised to 0.75% of GDP (from 0.5%). The Revenue Bill must be approved by the Senate by October 31. Although the arithmetic of the Chamber's modified package adds up to cover the fiscal gap anticipated for 2010, it raises the reliance on a higher fiscal deficit and public debt issuance. The modified revenue budget will be significantly weaker and more ad-hoc than the GOM's original proposal. It is doubtful that the measures are strong enough to avoid a ratings downgrade as this version stops short of providing a long-term solution to falling public revenue and will not help generate alternative income sources to replace the government's dependence on oil. (Mexico City)

14. (U) NUEVO LEON'S ECONOMY IS LOOKING UP AS EXPORTS INCREASE AND JOBS MOVE SOUTH: Unlike previous economic recoveries, where job creation in Mexico followed the United States, Mexico, and Nuevo Leon in particular, appear to be ahead of the US in creating new jobs in the wake of the economic crisis. According to recent statistics published by the state government, over 19,000 jobs were created in Nuevo Leon between June and September, many of them at the expense of American jobs. Manufacturers Whirlpool, Carrier, Ficoso and Navistar have all recently relocated production lines from the United States to Nuevo Leon, creating almost 2,000 new jobs here, but closing production facilities or eliminating jobs in Indiana, Texas, and Tennessee. Local job recovery has dovetailed with an increase in exports as the electronic, automotive, mineral, and electrical appliance sectors all saw double digit increases in exports from Nuevo Leon over the previous six-month period. (Monterrey)

15. (U) TOURISM FOREIGN CURRENCY INFLOWS DROP: As a result of the H1N1 flu and the economic crisis, Mexico registered an accumulative loss of USD 1.76 billion in tourism inflows (from January through August). The government and the private sector expect total losses for 2009 could reach USD 2 billion. The Bank of Mexico reported October 14 that from January through August, tourism inflows dropped 18.01% from USD 9.47 billion

during the same period of 2008 to USD 7.76 billion. Average spending per person fell 10.83% from USD 153 to USD 136.44. Miguel Torruco, president of the National Tourist Confederation said Mexico will fall from 18 to 22 in the global ranking of countries with the largest tourism inflows. (Mexico City)

16. (U) STEEL INDUSTRY HIT HARD BY THE ECONOMIC CRISIS, CRIME, AND INTERNATIONAL COMPETITION: The Mexican steel industry has been deeply affected by the economic crisis, with production only at 30% of capacity through this year according to Jaime Martinez Gallegos, President of the Association of Mexican Foundries' Western Region. . Spokesman for Altos Hornos de Mexico, headquartered in Monclova, Coahuila, have told Consulate officers that after a disastrous 4th quarter 2008 and 1st semester 2009, sales of hot and cold roll products have picked up. The States of Nuevo Leon and Coahuila, where 70% of Mexico's foundries are located, have been particularly affected because of the downturn in the automotive industry and the increase in theft of scrap iron intended for production. The Mexican steel industry consumes about 900,000 tons of scrap iron per year, which is recycled by foundries for various uses, including the automotive industry, agriculture and domestic use. In addition to theft of scrap iron en route by rail from the United States, Gallegos said that his industry has been hurt by competition from China and India, the fastest-growing markets for scrap iron. (Monterrey)

LABOR

17. (SBU) SINDICATO MEXICANO DE ELECTRICISTAS (SME): THE CONFLICT LOSES ENERGY AS IT GRINDS ON: The 150,000-person march on October 15 was the last show of force the SME will be able to make despite its calls for a national strike, according to Embassy contacts. Question about

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the legality of the decree ending the power company Luz y Fuerza del Centro (LFC) have been sent to committee by the House of Deputies for discussion. One Laboff contact believes this will release political pressure and provide the majority parties in the Congress a means to end the issue quietly. The government seems well prepared for the risk it took in ending one of the strongest and oldest unions in the country: severance packages are being paid, service is still delivered, and the protests are dying down. On its side, SME leadership is keeping up the rhetoric of the oppressed workers and drawing some attention from radical groups. There is, however, a legitimate concern about union autonomy in part of this process, and other powerful unions are watching developments carefully. The manner in which this issue is resolved will set a precedent for future union-government relations, and it is in the government's interest to see it finished well. (Mexico City)

18. (U) UNION AUTONOMY AND LABOR RIGHTS: Participants at an AFL-CIO Solidarity Center and the Friedrich Ebert Foundation conference on employer protection contracts October 15 called for union solidarity to support new organizing efforts, the miners' union (on strike now for three years), and the electricians' union recently dissolved by the federal government. The conference presented a series of radical speakers interspersed with case studies of young people who had become active in organizing in their workplaces as a result of abuses, real and perceived. The primary themes of the conference were threats to union autonomy, the need for union solidarity against the federal government and private enterprise, and the sorry state of the employment situation in Mexico. (Mexico City)

TRADE AND INVESTMENT

¶9. (U) STREAMLINING TRADE PROCEDURES: Through financing from the World Bank for USD 10 million, Mexican Customs is working to revamp its procedures and simplify trade procedures. The simplification process is expected to conclude in 2011. Through this process, importers and exporters will be able to conduct their operations through one government office. Customs is currently drafting the bids for the companies that will develop the software and conduct the re-engineering process. The burdensome customs procedures increase trade costs, which makes Mexican exporters less competitive than China. According to the media, Mexican exporters are realizing cheap labor costs are not enough to compete against China and wish to take advantage of the fact that China is losing its comparative advantage with the appreciation of the yuan. (Mexico City)

¶10. (U) GRUPO ALFA REPORTS STRONG THIRD QUARTER: Monterrey-based conglomerate Grupo ALFA reported third quarter earnings (EBITDA) of \$290 million dollars, a 14% increase over the same period last year and 9% over the second quarter of this year. Quarterly sales increased by 9% to \$2.2 billion dollars. Noting that this is the second consecutive quarter with earnings at pre-crisis levels, President Dionisio Garza Medina said it was ALFA's strongest quarter as measured by EBITDA and that he is confident ALFA will negotiate its way through the economic crisis and be well-positioned for long-term growth. ALFA is the world's leading manufacturer of high-tech aluminum engine blocks and is a leading petrochemical producer. Headquartered in Monterrey, it is divided into four business groups: Alpek (petrochemicals), Nemak (aluminum auto components), Sigma (refrigerated food) and Alestra (telecommunications) and has operations in 17 countries. (Monterrey)

¶11. (U) BEST BUY'S EXPANSION INTO MEXICO OFF TO STRONG START: The American electronics store Best Buy opened its first store in Jalisco just over two weeks ago, but its unexpectedly strong sales have already caused the company to overhaul its logistics and restocking plans. The opening on October 2 is Best Buy's second store in

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the country, following its launch in Mexico City last year. The company sold a month and a half's worth of goods in the store's first week, putting sales three times higher than expectations. Best Buy will open its second store in the Guadalajara area in early 2010 and decided to expand its warehouse at that location to make the stores less dependent on stocks in Mexico City. In addition, the company plans to open three more stores in the Mexico City area to have five by the end of this year. (Guadalajara)

TRANSPORTATION AND INFRASTRUCTURE

¶12. (U) QUARTERLY BAJA CALIFORNIA PORTS OF ENTRY BORDER LIAISON MECHANISM (BLM): The October 13-14 meetings regarding the San Ysidro/El Chaparral Otay Mesa, Otay Mesa East, and Mexicali/Calexico projects revealed the usual frustrations over mismatched timelines (GOM wants US to accelerate timelines, particularly for San Ysidro and Otay East) and placement and number of pedestrian

crossings at San Ysidro /El Chaparral. On the latter, the Mexicans have agreed to the U.S. request for two south-bound pedestrian crossings, but the General Services Administration (GSA) and its Mexican partner agency, INDAABIN, are still working out technical issues regarding their placement, and the U.S. denied Mexico's request for "reciprocity" and will not create two northbound crossings due to CBP staffing issues. Land acquisition and right-of-way issues continue to be problems on both sides of the border for San Ysidro and both Otay projects. Calexico and Mexicali officials were disappointed to find the timeline for that project pushed back another year, and the number of southbound vehicle lanes reduced to five, though GSA says studies suggest this will not create traffic backups in Calexico. The BLM is beginning to discuss moving forward on a Port of Entry renovation project in Tecate, though CBP was not available at the meeting, limiting discussion. (Tijuana)

ENERGY AND ENVIRONMENT

¶13. (SBU) MEMBERS OF CONGRESS CHALLENGE CONSTITUTIONALITY OF ENERGY REFORM REGULATIONS: The Mexican Chamber of Deputies (with a majority of opposition PRI and PRD members) has presented before the Supreme Court a constitutional challenge against the implementing regulations of the energy reform bill which were released by the Calderon Administration in September. PRI and PRD deputies are challenging the articles in the regulations which would allow the administration to pay service contracts based on productivity, capacity and production. The Secretariat of Energy and Pemex have been working to develop the new performance based service contracts for exploration and production with this regulation being a key to attracting interest from international oil companies, and increasing Pemex' flexibility and efficiency. Pemex had hoped to issue the first round of bids under the new service contracts early in 2010. Embassy contacts expect the appeal could delay that process by six to eight months. This is a sobering development for the Calderon Administration which had hoped to use the new performance based contracts to enhance exploration and development activities in the deepwater of the Gulf of Mexico. (Mexico City)

¶14. (U) CFE TO TAKE OVER ELECTRICITY SERVICE IN MEXICO CITY: The Energy Ministry (SENER) said it will leave the state-run Federal Electricity Commission (CFE) in charge of power distribution in and around Mexico City following the recent shutdown of the Luz y Fuerza del Centro utility (LFC). SENER said the decision by President Calderon guarantees that electricity service will remain

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in state hands. Citing annual losses running into USD billions and lack of efficiency, Calderon decreed the shutdown of LFC, which distributed electricity in Mexico City and parts of the central states, but stressed that electricity will not be privatized. The government previously had been considering creating another state company to replace LFC, which employed 44,504 people. (Mexico City)

¶15. (U) SONORA SEEKS WATER TO MAINTAIN GROWTH: Governor Padres announced on Tuesday, October 20 a historic budget proposal of 2.43 billion pesos to invest in exploration of new water sources, which is a 291 percent increase from the previous year. According to an August report by CONAGUA, current reservoirs are 71 percent of capacity due to increased population growth in the cities and less than average rainfall over the last decade. State officials are concerned about sustainable development as

Sonora relies on its heavily irrigated agricultural industry as the backbone of its economy. (Hermosillo)

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